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No. 86-147

In The

Supreme Court of the United States

October Term, 1986

HOME WARRANTY CORPORATION, HOME OWNERS WARRANTY CORPORATION, and HOW INSURANCE COMPANY,

Petitioners,

v.

JOHNNIE L. CALDWELL, Insurance Commissioner of the State of Georgia,

Respondent.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether denial of the Petition is appropriate in light of the decision of the Eleventh Circuit Court of Appeals to vacate the entry of summary judgment and remand to the district court for further clarification of the record.

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Respondent, the Insurance Commissioner of the State of Georgia, respectfully opposes the Petition for a Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit. The court of appeals correctly vacated the decision of the district court granting summary judgment to the Petitioners as lacking sufficient factual support in the record, and correctly remanded the case to the district court for further development and clarification of the record.

STATEMENT OF THE CASE

A. Proceedings Below

This action was filed in the United States District Court for the Northern District of Georgia by HOW Insurance Company ("the Company" or "HOWIC") and two of its corporate parents, Home Warranty Corporation and Home Owners Warranty Corporation ("HOW") (collectively, the "Petitioners") seeking declaratory and injunctive relief against the Respondent, Johnnie L. Caldwell, Insurance Commissioner of the State of Georgia ("Commissioner").[1] More specifically, the Petitioners sought a determination that their activities within the State of Georgia are exempted by the Risk Retention Act, 15 U.S.C. § 3901 *et seq.*, Petitioners' Appendix, p. 102a, from the Commissioner's normal regulatory authority over insurance companies operating in the State, and further sought an injunction preventing enforcement of a cease and desist order issued by the Commissioner on April 19, 1983 (the "Commissioner's Order").

On May 13, 1983, the district court entered a preliminary injunction enjoining the enforcement of the Commissioner's Order and enjoining the Commissioner from taking any regulatory actions vis-a-vis Petitioners except those set forth in 15 U.S.C. § 3902(a)(1)(A)-(G). The Commissioner appealed the entry of the preliminary injunction to the court of appeals, but that appeal was dismissed as moot, after briefing and oral argument, when the Court below entered a permanent injunction.

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[1]Warren D. Evans has succeeded Johnnie L. Caldwell as Insurance Commissioner since the filing of the action. Respondent is not a corporation and thus no filing has been made under Rule 28.1.

In entering a permanent injunction on July 23, 1984, the district court granted Petitioners' motion for summary judgment and concluded as a matter of law that HOW's insurance program fell within the confines of the Risk Retention Act, relying, without any amplification, upon the United States District Court of Delaware's decisions in *Home Warranty Corporation, et al. v. Elliott,* 572 F.Supp. 1059 (D. Del. 1983) ("*Elliott* I") and 585 F. Supp. 443 (D. Del. 1984) ("*Elliott* II"); Pet. App. at pp. 73a, 75a, 83a. The permanent injunction restrained the Commissioner from enforcing his cease and desist Order and from "otherwise interfering or attempting to interfere or restrict [the Company] . . . from underwriting the HOW program and issuing HOW product liability insurance in the State of Georgia." Pet. App. at 74a.

The Commissioner appealed the entry of the district court's order granting summary judgment to the United States Court of Appeals for the Eleventh Circuit. After considering oral argument and briefs of counsel, the Court below vacated and remanded, finding that Petitioners' motion for summary judgment "does not provide undisputed facts to show: (1) whether products liability risks of the member builders are retained and spread; (2) whether retention and spread of products liability risks of the members is the primary purpose of the group." *Home Warranty Corp., et al. v. Caldwell,* 777 F.2d 1455, 1489 (11th Cir. 1985); Pet. App. at p. 70a.

Petitioners' motion for rehearing en banc, which raised essentially the same arguments as are posited in the Petition, was denied by the court of appeals on June 16, 1986. Pet. App. at p. 71a.

B. The Risk Retention Act

In 1981, the United States Congress adopted the Risk Retention Act as a mechanism to address the rising cost of product liability insurance to manufacturers, distributors and sellers of products, by permitting such persons to purchase insurance on a group basis, or to self-insure through insurance companies called "risk retention groups." 15 U.S.C. § 3901, *et seq.*, House Rep. No. 97-190, 97th Cong., 1st Sess., *reprinted in* 1981 U.S. Code Cong. & Ad. News (95 Stat.) 1432.

The term "insurance" is defined by the Risk Retention Act to include "primary insurance, excess insurance, reinsurance, surplus lines insurance, and any other *arrangement for shifting and distributing risk* which is determined to be insurance under applicable State or Federal law." 15 U.S.C. § 3901(a)(2) (emphasis added).

The term "product liability" is defined to mean:

> "*liability for damages* because of any personal injury, death, emotional harm, consequential economic damage, or property damage (including damage resulting from the loss of use of property) arising out of the manufacture, design, importation, distribution, packaging, labeling, lease or sale of a product . . . ." 15 U.S.C. § 3901(a)(3) (emphasis added).

A "risk retention group" is defined by the Act as:

> " . . . [a] corporation . . . formed under the laws of any State . . .
>
> (A) whose *primary activity consists of assuming and spreading all, or any portion, of the product liability . . . risk exposure of its group members;*
>
> (B) which is organized for the primary purpose of conducting the activity described under subparagraph (A);

(C) which is characterized or licensed as an insurance company and authorized to engage in the business of insurance under the laws of any State . . .; [and]

* * *

(E) which is composed of members each of whose principal activity consists of the manufacture, design, importation, distribution, packaging, labeling, loan, or sale of a product or products." 15 U.S.C. § 3901 (a)(4) (emphasis added).

The key substantive provisions of the Risk Retention Act, and the provisions at the center of the instant dispute, provide that a risk retention group is substantially exempt from most state laws, rules, and regulations, or orders relating to commercial insurance, except that the group must be chartered or licensed in any one state. 15 U.S.C. § 3901(a)(4)(C); 15 U.S.C. § 3902(a)(1).

While the Act allows some limited regulatory activity by a non-chartering state, an entity that achieves risk retention group status under the Act may, nevertheless, operate as an insurance company in a state without the normally required certificate of authority from that state and without being subject to the bulk of regulation, financial and otherwise, imposed by the various states upon insurance companies. In Georgia, this regulation includes requirements, inter alia, that insurance companies be licensed (O.C.G.A. § 33-3-2); that insurance companies make deposits for the benefit of insureds in the event of an insurance company's insolvency or failure to pay a claim (O.C.G.A. Chs. 33-3, 33-12 and 33-37); that the Georgia Insolvency Pool pay claims made against licensed insolvent insurance companies by Georgia insureds (O.C.G.A. Ch. 33-36); that policy forms be approved and contained certain provisions for the public's protection (O.C.G.A. Ch. 33-24); that insurance companies refrain from certain

specified unfair trade practices affecting the public (O.C.G.A. Ch. 33-6); that insurance be sold only by licensed agents who are subject to various educational and ethical requirements (O.C.G.A. Ch. 33-23); that insurance companies have initially and maintain a specified minimal level of capital and surplus (O.C.G.A. §§ 33-3-6, 7); and that insurance companies submit to regular financial examinations (O.C.G.A. § 33-2-11).

C. The HOW Program and Delaware Litigation

The HOW Insurance Company is not licensed as an insurance company in the State of Georgia and, in fact, is so licensed only in the State of Delaware. Subsequent to its licensing in Delaware, the Company filed its insurance program, as marketed in Georgia, with the Insurance Commissioner of Delaware. While the Delaware Insurance Commissioner did not disapprove the filing, he expressly concluded on March 4, 1982, that it was inappropriate to deal with the filing under the Risk Retention Act and therefore forbade use of the filing by HOW as a basis for offering the program in other states under the provisions of the Act. On August 4, 1982, the Delaware Insurance Commissioner affirmed his earlier determinations concerning HOW's insurance program. However, in subsequent litigation between the Petitioners and the Delaware Insurance Commissioner, to which the Georgia Insurance Commissioner was not a party, the District Court of Delaware held that HOW and HOWIC's activities were within the Risk Retention Act. *Elliott* II, *supra*, 585 F.Supp. at 443; Pet. App. at 82a. The Delaware district court's decision was not appealed.

HOW's program, as filed in Delaware and as promoted in Georgia, appears to operate as follows:[2]

1. A home builder participating in the Home Owners Warranty program makes certain express one and two-year warranties to the consumer/purchaser of a home built by the participating builder.

2. The HOW Insurance Company issues to the home purchaser a "Certificate of Insurance," physically resembling an insurance policy, which insurance purports to underwrite the builder's express warranties during the first two years after sale, and insures the home against certain structural defects during the third through tenth years after the purchase of the home.

3. Under the "Certificate of Insurance" issued by the Company to the home purchaser, all claims are to be made by the consumer/purchaser directly against the Company; all benefits, if any, are to be paid by the Company directly to the home purchaser and all deductibles are to be paid by the consumer/purchaser. The home purchaser must assign to the Company his rights under other insurance policies held by the purchaser.

4. HOW's program is promoted and marketed to home purchasers as an inducement to purchase a home built by a participating builder, and the purchaser must sign the application in order for the coverage to become effective. While the cost of the program is initially borne

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[2]This recitation of the elements of the HOW program is necessarily confined to the structure of the program as it existed in 1984 and to those elements which can be gleaned from the record. The operation of some portions of the program is unclear from the record, as discussed below.

by the home builder, it is subsequently passed on to the purchaser.

5. At least as to the one and two-year builder warranties, the Company has the right to obtain reimbursement from the defaulting home builder for any claims paid to the consumer/purchaser. The limits of the insurance coverage on years 3 through 10 are reduced by any payments made by the Company as a result of builder default on the warranty.

In Georgia, 34% of the claims numerically and 44% of the dollar amount of claims paid by the Company for the period March 1, 1982 through April 30, 1984, have been under the one and two-year builder warranties.

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SUMMARY OF ARGUMENT

The court of appeals properly framed the issue to be decided. The court was unable to dispositively decide the issue, however, because the record below is unclear and contains unresolved internal inconsistencies. The court of appeals had no choice but to vacate the entry of summary judgment for the Petitioners and to remand to the district court for further proceedings, based upon the absence of undisputed facts in the record sufficient to warrant granting the motion. The lack of clarity in the record thus makes the Petition premature, and logically suggests further development of the record in the lower courts.

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ARGUMENT AND CITATION OF AUTHORITY

A. The Court of Appeals Properly Framed the Issue.

At the outset of its exhaustive and scholarly opinion, the court of appeals perceived the practical importance of its task: "Most immediately at issue is the validity of an insurance marketing enterprise with outstanding insurance contracts valued at $70.000,000,000." *Home Warranty Corp. et al. v. Caldwell*, 777 F.2d 1455, 1457 (11th Cir. 1985); Pet. App. at 2a.

Seeking to ground its opinion "upon the broadest range of information available to us," the court of appeals painstakingly traced the evolution of products liability law in the United States. *Id.* at 1457; Pet. App. at 3a. In its historical perspective, the underlying rationale of products liability, as well as the linchpin of the federal Act being construed, is the assumption and distribution of risk. *Id.* at 1460; Pet. App. at 9a.

The court of appeals examined the economic consequences of the expansion of products liability law, including the increased reliance upon product liability insurance "as a means of leveling the costs of unpredictable awards, the usual function of insurance as risk distribution." *Id.* at 1462; Pet. App. at 14a. Partly because of rate-making procedures of liability insurers, partly because of unsafe manufacturing practices and partly because of uncertainties in the judicial and statutory treatment of product liability claims, an apparent "problem" arose in the field of product liability in the late 1970's. *Id.* at 1463; Pet. App. at 15a. The "problem," perceived by some as a "crisis," set the stage for passage of the Risk Retention Act of 1981. *Id.* at 1463-4; Pet. App. at 15a-17a.

What emerged from the Congressional inquiry into the products liability "problem" was a new insurance concept authorizing the formation of "risk retention groups," which would provide insurance only to their members and insure only products liability and completed operations hazards. *Id.* at 1467; Pet. App. at 23a. It was recognized that some preemption of state law would be required to effectuate the plan, with the original intent being to allow interstate insurance capability to inject an element of competition to modify the existing subjective rate-making policies of product liability insurers. *Id.* at 1467; Pet. App. at 24a.

From its inception, as the court of appeals noted, the federal approach to the "problem" was predicated upon restricting the scope of preemption by limiting the field of customers that risk retention groups could serve:

> "Risk retention groups were member financed and member servicing organizations only; the state's interest in regulating insurers dealing with the public was to remain untouched by this legislation." *Id.* at 1468; Pet. App. at 26a-27a.
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> "Risk retention groups were appropriately exempted from state regulation of insurance companies because risk retention groups were not in the business of selling insurance to the public." *Id.* at 1472; Pet. App. at 35a.

Against this backdrop of legislative history evidencing an intent that risk retention groups not engage in the business of selling insurance to the public, the court of appeals raised the question of:

> ". . . whether an insurance organization selling what Georgia law would characterize as a home owner's policy may, by virtue of federal law, insure homes sold to Georgia home owners without complying with otherwise applicable Georgia insurance regulations." *Id.* at p. 1457; Pet. App. at 2a.[3]

In responding to its question, the court concluded that even if the subject matter of HOW's insurance did fall within the scope of the Risk Retention Act, *Id.* at 1487; Pet. App. 67a, the court would focus on the orchestration of the program to determine "whether the 'primary activity' of the entity in question consists of the assuming and spreading of the product liability risk of its group members." *Id.* at 1479; Pet. App. at 49a.

The court agreed with the district court in *Elliott I, supra,* 572 F.Supp. 1059, that the coverage provided during the first two years of the HOW program does *not* constitute assumption and spreading of the product liability risk exposure of its member builders, and instructed the trial court to exclude that segment of HOW's activity in calculating the portion of the program which insures the product liability risks of its members. *Id.* at 1487; Pet App. at 67a-68a.

Turning to the remainder of the HOW coverage, years 3 through 10 of the program, the court considered not only

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[3]The Delaware district court, which ultimately sustained HOW's contentions, nevertheless acknowledged that "[i]f it were factually true that this portion of the HOW program [coverage for years 3-10]were in substance a sale of property loss coverage to homeowners, [the Commissioner of Delaware's] position would have to be sustained." *Elliott I, supra,* 572 F. Supp. at 1066; Pet. App. at 98a (parenthetical added).

whether the program sufficiently constituted the insuring of products liability risks, but also whether HOW actually assumed *any* of the liability of its members, given the lack of any undertaking in the HOW policy running to or protecting the member builder. *Id.* at 1488; Pet. App. at 68a. Having framed the issue to be decided and rhetorically analyzed the structural composition of the program, the court stopped short of reaching a final determination of the questions presented. *Id.* at 1489; Pet. App. at 70a.

B. The Court of Appeals Correctly Remanded to the District Court.

The court of appeals was unable to unravel the HOW puzzle, noting that "[t]he record is far from clear" on HOW's assumption of liability of its members. *Id.* at 1488; Pet. App. at 68a. The court further noted "tensions," or internal inconsistencies, among the materials offered by HOW in support of its motion for summary judgment, such as the representations in the affidavit of the Company's president that payments are made to homeowners "on behalf of" the builder members and that the Company will "defend" builders against claims by the homeowner, contrasted with the lack of any such undertakings in the HOW insurance policy. *Id.* at 1488; Pet. App. at 69a-70a.[4]

The court concluded that the record did not provide sufficient undisputed facts to support the district court's decision granting the motion for summary judgment in HOW's favor. *Id.* at 1488-89; Pet. App. at 70a. Upon re-

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[4]HOW continues to argue that it indemnifies the builder in its statement of the case submitted to this Court. Pet. Brief, p. 6.

mand, the district court was instructed to develop the record to determine: "(1) whether products liability risks of the member builders are retained and spread; (2) whether retention and spread of products liability risks of the members is the primary purpose of the group." *Id.* at 1488-89; Pet. App. at 70a.

C. The Petition is Premature.

This Court has previously stated that "[w]ise adjudication has its own time for ripening." *Maryland v. Baltimore Radio Show*, 338 U.S. 912, 918 (1949).

While it is apparent from the breadth and depth of the court of appeals' opinion that this case raises important questions of federal law, the court of appeals was unable to reach a definitive conclusion as to whether the nature of HOW's undertakings and the "orchestration" of its program are such as should entitle it, on the basis of the existing record, to claim the benefits of the Risk Retention Act. *Home Warranty Corp., et al. v. Caldwell, supra*, 777 F.2d at 1487; Pet. App. at 67a. The court found the underlying factual record to be clouded, and determined that further illumination at the district court level would be required. *Id.* at 1488-89; Pet. App. at 70a. The same rationale supports the denial of the Petition for Writ of Certiorari. *See Maryland v. Baltimore Radio Show, supra*, 338 U.S. at 918. Rule 17, United States Supreme Court.

Contrary to Petitioners' assertions, the court of appeals has not "engrafted" any additional qualifying criteria in interpreting the Act. Pet. Brief, p. 9.[5] The court

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[5]The same argument was raised by Petitioners in their Petition for Rehearing and Suggestion for En Banc Consideration before the court of appeals, and was rejected. Pet. App. at 71a.

merely recited some factors which it considered relevant in the determination of whether the Petitioners' primary activity is the assumption and spread of the products liability exposure of its members. *Home Warranty Corp. et al. v. Caldwell, supra*, 777 F.2d at 1488; Pet. App. at 68a.

The HOW insurance policy, itself, apparently is insufficient to provide an answer, not only because it conflicts with statements made by the Company's president in a sworn affidavit, but also because the policy undertakes to pay for certain losses suffered by the homeowner without regard to the builder's legal liability therefor. *Id.* at 1488; Pet. App. at 69a-70a.

Petitioners confuse the court of appeals' attempt to clarify the record with subversion of Congressional intent. At numerous points during the lengthy opinion, the court below exhibits mindfulness of its duty "to apply the Act as it is written and thus . . . defer any subsequent remedial measures to the legislative process." *Id.* at 1486; Pet. App. at 64a.

It would thus be a premature and potentially wasteful exercise of this Court's jurisdiction to embark upon a determination of the applicability of a federal statute to an unclear and inconsistent factual record.[6]

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[6]Furthermore, amendments to the Act, itself, are currently pending in Congress. See S. 2129 (99th Congress); Pet. Brief, p. 16.

CONCLUSION

The court of appeals decision to remand the case is correct. The Petition is premature in light of the uncertainty in the record, such that further proceedings in the lower courts are appropriate prior to any review by this Court. The Petition should be denied.

Respectfully submitted,

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